



CITY COUNCIL AGENDA REPORT

May 1, 2013
Assistant City Manager

TITLE: JOINT WORKSHOP WITH THE HOUSING COMMISSION TO DISCUSS CITY AFFORDABLE HOUSING POLICIES RELATED TO NEW MULTI-FAMILY RENTAL RESIDENTIAL DEVELOPMENT

SUMMARY

At your meeting of April 16, 2013, the City Council approved a joint workshop with the Housing Commission for the purpose of discussing Policy 16 of the City Housing Element that anticipates both a review and modification of the Inclusionary Zoning Ordinance (IZO) to assure conformance with City goals, state legislation, including the Costa-Hawkins Act, and recent court rulings including the *Palmer/Sixth Street Properties L.P. v. City of Los Angeles ("Palmer")* case. As such, this workshop is intended to review existing City policy related to affordable housing, the overall legal environment and a number of staff and Housing Commission concepts for amending the IZO. In addition, staff anticipates the City Council will provide direction regarding IZO amendment timelines and the most appropriate approach for continuing to process affordable housing agreements during the time that the IZO is undergoing the amendment process. Attachment 1 to this report is the April 16, 2013, agenda report concerning the purpose of this workshop which provides background information.

RECOMMENDATION

1. Identify one or more of the five IZO amendment option(s) as detailed in this report, or one that emerges from the workshop, that should be the focus of the IZO amendment process.
2. Indicate acceptance or modification to the project time line as outlined in this report for completing the IZO update process. Staff estimates the amended IZO and related material could be presented to the City Council in September/October.
3. Identify one of the interim negotiating options outlined in this report, or one that emerges from the workshop, for addressing developer requests to negotiate an affordable housing agreement. This interim approach would be in place until the City Council formally amends the IZO. Staff is recommending interim negotiation process #2 involving continued negotiations in an attempt to obtain satisfactory project affordability.

FINANCIAL STATEMENT

There is no direct financial impact to the City as a result of this action.

BACKGROUND

The City's IZO was adopted to establish a clear and attainable plan for using the limited remaining developable land in a manner that is consistent with City housing policies. To that end, the IZO establishes that 15% of all units in a new residential multi-family rental development in excess of 15-units shall be rent-restricted to very low (50% of the Area Median Income or AMI; currently \$44,600 for a four person household) and low income households (80% of the AMI; currently \$71,350 for a four person household) and that 20% of all units in a new residential ownership development be made available to very low, low income households and/or moderate income (120% of the AMI; currently \$105,050 for a four person household) households. In addition while the IZO is clear in stating that its goal is to obtain affordable inclusionary units, it does recognize that this may not always be practical and as such, it lists alternatives including:

- Provide for inclusionary units at a location within the City other than the project site
- Dedication of land to a non-profit housing developer for development of affordable units
- Credit transfers that allow one unit with an excess in the number of affordable units to make them available to another development
- Other alternatives approved by the City

In addition to the above, upon City approval, an applicant may pay the City's Lower Income Housing Fee (LIHF) which is currently \$2,655/unit for rental developments and single family homes under 1,500 sf in lieu of providing affordable units. The fee for single family homes in excess of 1,500 sf is currently \$10,713/unit and the fee for commercial development is \$2.83 per sf. It should be noted that in accordance with long term practice, the fee option is considered only after all other options are determined to be impractical.

In addition to these alternatives, the IZO also outlines incentives the City may offer to assist with obtaining inclusionary units including, fee waivers, design modifications such as reduced setbacks and landscaping, second mortgages and other City financial assistance, and priority permit processing.

In addition to the IZO, in July 2010, the City Council adopted Resolution 10-390 which states in part, the City will act affirmatively to promote development of well designed affordable housing for families with children and the construction of affordable three bedroom units for large families (Attachment 3).

Current IZO Environment

In general, the most significant issue regarding the IZO is that there is currently a "disconnect" between the requirement that 15% of all units in a new residential multi-family rental development be rent-restricted and the *Palmer* case which held that local inclusionary requirements requiring rent restricted units violate the Costa-Hawkins Act that allows landlords to set the initial rent for a new unit and to adjust rents to market levels whenever a unit is vacated (so-called "vacancy decontrol").

This disconnect is also evident between the City's *Housing Site Development Standards and Design Guidelines* which require compliance with the City's IZO and the "by right" aspect of high density rental housing.

Finally, the City is expected to implement a range of Housing Element programs that should, if appropriately applied, lead to meeting state mandated and RHNA housing and affordable housing targets. However, absent strict IZO requirements, it is doubtful that new affordable housing units will approach these targets. Regarding this matter, as evidenced in the table below, even in the best of situations, meeting RHNA targets is impractical within the current housing market.

SUMMARY OF CURRENT AND DRAFT RHNA

Income Levels	2007 – 2014 Adopted RHNA	2014 – 2022 Draft RHNA
Very Low (50% AMI)	1,076	713
Low (80% AMI)	728	389
Moderate (80% to 120% AMI)	720	405
Above Moderate (+120% AMI)	753	551
TOTAL UNITS	3,277	2,058

As an example, assuming that the California Center, St. Anton and Auf der Maur developments each met its affordability goals by providing all 15% of their inclusionary units at very low income, a total of 117 very low income units would be provided. Notwithstanding this situation, the City is obligated to carrying out its Housing Element that is designed to meet both RHNA goals and state housing policies requiring cities to demonstrate how they will meet existing and projected housing needs for all income categories.

Affordable Housing Rent Calculations

Prior to reviewing available options for amending the IZO, it's important to note that the generally accepted definition of affordability is to provide housing so that a household pays no more than 30 percent of its monthly income on housing (i.e., rent or mortgage). Families who pay more than 30 percent of their income for housing are considered cost burdened and may have difficulty affording necessities such as food, clothing, transportation and medical care. As a way of fine tuning the definition, HUD established various generally accepted income categories of very low, low, median and moderate which are used as identifiers for various income levels. Further, these general income levels are categorized by household size. (Attachment 3 details the recent HUD income figures.) As a result, providing affordable housing units includes establishing a rent structure that is no more than 30% percent of a household's income based on annual income and household size.

One common variation to the above standard is that while household size is always consistent when determining annual income qualification (that is a three person household must meet the income requirements for a three person household), the

actual rent calculations are generally set on a negotiated preset household size regardless of the number of individuals residing in a unit. As an example, while a rent for a two bedroom unit may be based on a three person household, the unit could be leased to a two or four person household all of which would pay the same rent. A sample of the rent calculations are as follows:

Rent and Income Calculations

- 50% AMI with 2 Person Household: \$35,700
- 50% AMI with 3 Person Household: \$40,150
- Rent for a two-bedroom unit based on a two person household: $\$35,700 / 12 \text{ months} = \$2,975 * 30\% = \$893/\text{mo}$
- Rent for a two-bedroom units based on a three person household): $\$40,150 / 12 \text{ months} = \$3,345 * 30\% = \$1,004/\text{mo}$

As a result of the above, staff's affordability efforts regularly focus on setting not only income categories, but household sizes to determine rents. Also, while the IZO sets household size for each type of unit by bedroom size, staff has historically negotiated the household size/rent amount with developers as a means of obtaining the largest amount of affordability.

The table below lists a sampling of market rents as compared to standard affordable rent for a one bedroom apartment.

Survey of Market Versus Affordable Rents ⁽¹⁾

Complex	Estimated Monthly Rent
Stoneridge Apartments	\$1,540 to \$1,652
Kensington Apartments	\$2,280 to \$2,340
Archstone Hacienda	\$1,755 to \$1,985
Avalon Bay (Dublin)	\$1,830
Affordable at 50% AMI	\$893
Affordable at 80% AMI	\$1,428
Affordable at Median (100%)	\$1,784

1. Market rents obtained from phone survey on April 22, 2013

IZO Amendment Options

Staff's overall impression is that the IZO has been a useful tool for acquiring inclusionary affordable housing and as such, potential amendments are intended to address legal matters and City Council objectives without, most likely, a complete rewrite of the ordinance. However, as noted above, as it relates to rental unit requirements, it is in conflict with *Palmer*. Nevertheless, the concepts below are intended to be comprehensive and stand alone by themselves however; they can be combined or amended to meet objectives. All of the options below were discussed at the Housing Commission's April 9 workshop and it felt them appropriate for discussion at this joint workshop.

1. Amend Section 17.44.040 by removing the very low and low income 15% affordability requirement and replace it with either or a combination of:
 - a. A lower percentage of affordable units, such as 12%.
 - b. Replace the requirement for a specific percentage of affordable units with a statement indicating that the developer and city will negotiate an appropriate level affordability with a City goal/target of 15% affordable to very low and low income households.
 - c. Both (a) and (b) could be augmented so that for every one percent less than 15%, the project would pay the LIHF for 7% of the development's total units. As an example, if a development provided 10% affordable units in the low and very low income categories, it would also pay the LIHF on 35% of the total project's units ($15 - 10 = 5 \times 7 = 35\%$ of the total units required to pay the LIHF).
 - d. Allowing up to a certain percentage of the affordable units (perhaps 35%) to be affordable to households at the median income. In addition, this option could be combined with requiring only a minimum number of very-low (3%) and low income (4%) units and an accompanying LIHF component for median units.

The effect of the above is that the City retains the basic structure of the IZO but sets standards and targets that are more easily attainable and more likely to be agreeable to developers. The downside of these alternatives is that both (a), (c), and (d) would continue to be in conflict with *Palmer* and thus a developer could potentially refuse to meet them or exercise their legal rights which would leave the City with few options for meeting affordability.

2. Explore the potential for providing housing for lower income households without implementing rent restrictions. With this option the property is required to provide evidence that a certain percentage of its units are occupied by very low income or low income households. In most cases, meeting this target results in a large percentage of the households paying more than 30% of their income for rent. However, in theory, it leads to "market" adjustments to assure that the affordability targets are met and it can open the door for lower income households obtaining rental units in Pleasanton. This option is currently in place at the Gatewood Apartments located on Stoneridge Drive.

While this option may lead to some reduced rents, there is little motivation to establish rents consistent with 30% of annual income. As such, it would most likely have minimal impact in addressing affordable housing needs. Further, developers may view this as veiled rent control and thus, raise legal objections. Finally, project monitoring would be difficult and its doubtful that this option would be considered as providing affordable units that could be counted toward meeting the City's RHNA as it requires rent restricted units.

3. Shift attention from inclusionary units to maximizing affordable housing fee payments/revenue to purchase or construct unit affordability. As indicated, the LIHF nexus study that is underway (and scheduled for completion in August/September) will identify a supportable fee that is closer to offsetting the impact (i.e., based on mitigating the impact) of not providing affordable units and attempt to create a legally sustainable nexus and as such, it should provide revenue that could be leveraged to acquire affordable units.

For this option to be effective, the City Council would need to set the fee at an amount that is at or closer to the amount that will be recommended in the study rather than retaining the modest fees currently in place. Also, once the fees are paid, the City would need to identify opportunities to acquire property for developing a City driven project, partner with a developer that is willing to include inclusionary units in its development or provide a developer with financial incentives for enhancing project affordability. One issue with the latter option is that developers have recently been hesitant to accept financial contributions from the City since it may trigger State prevailing wage requirements. As such, the City's best effort would most likely be to pursue its own development, such as Ridge View Commons and the Promenade that involve partnering with a non-profit developer. This option also would allow the City to pursue the IZO's alternative approaches, such as land acquisition, off site housing, etc.

While a number of cities have moved to this option as a way of complying with *Palmer*, the sustainability of the fee is largely dependent of the quality of the LIHF nexus study and its overall acceptance in the development community. As such, fees are often approved well below the amount recommended in the nexus study which raises concern that the fee revenue will be adequate to develop any significant amount of affordable housing.

4. This Option involves establishing a new zoning designation for Nonprofit High Density Residential, Mixed Income (NHDRMI) requiring that all properties the City identified for high density residential development (30+units/acre) receive a NHDRMI zoning designation. Zoning requirements include the property owner designating a nonprofit provider that would control the site and develop at least 40% of the residential units. The nonprofit would also select the for profit developer that would develop the remainder of the site's units.

As outlined in the Citizens for a Caring Community correspondence dated April 8, 2013, (Attachment 4), which has recommended this option, it would focus on creating mixed income neighborhoods rather than mixed income households within buildings. Further, because there would most likely be a separation of buildings designating affordable and market, it could better qualify for tax credits and other funding options. In essence, it allows the market developer to focus on its expertise that is providing market rate housing, while allowing the nonprofit to focus on its expertise, which is providing affordable housing. Citizens for a Caring Community is careful to point out that this option would not necessarily lead to 100% affordable buildings, which has been a concern of the City Council, but could have some mixture of incomes in the nonprofit

buildings. Nevertheless, to make the option feasible, there would be “affordable buildings” that would house the majority or all of the affordable households in the development.

Staff's review to date indicates significant legal issues with establishing zoning for a specific type of entity, e.g., requiring a non-profit specifically. The City Council may recall a similar dialogue regarding the Wal-Mart Neighborhood Market proposal in that cities cannot create zoning that would specifically ban Wal-Mart or similar corporations from developing or occupying a site where the proposed use is consistent with the zoning. Further, staff anticipates that this option would result in considerable financial contribution from the City since this is typically necessary to obtain the levels of affordability anticipated in this option.

While the City cannot legally zone a property to require a non-profit to develop part or all of a site, staff does see the value in promoting this type of nonprofit/for profit arrangement and would not hesitate adding it to the listing of alternatives to providing inclusionary units and to strongly encourage developers to work with nonprofits. Recently, the City of Dublin processed a development application that utilized this model whereby two developers, a nonprofit and a market developer, worked collaboratively to develop a single site.

5. Establish an affordable housing overlay zone designation that provides a density bonus, unique development standards or other benefit to accommodate a stand-alone affordable housing project or one that is combined with a market project. In general, this designation requires a high level of affordability concentrated in a specific building or portion of a site and, like option 4; its purpose is to have one portion of the development assume affordability for the entire development.

With this option, which has been adopted recently by Corte Madera and is being considered by Menlo Park, most of the development incentives included in the zoning overlay are included in our existing IZO and can be applied as needed to assist the project. (The exception is the option of a density bonus.) Further, staff has not received any feedback from developers indicating that the City's recently adopted development standards and design guidelines are creating impediments to providing affordable housing. As such, staff sees little advantage to pursuing it at this time.

Based on the above, staff recommendation includes the City Council identifying one or two of the above amendment options that staff would use during a public review process guided by the Housing Commission. In addition, during the workshop the City Council could identify additional or alternative options for staff review.

Housing Commission Processing Recommendations

As indicated above, at its April 9 workshop, the Housing Commission reviewed all of the above IZO amendment options but did not recommend specific ones in favor of having then considered as part of the workshop. However, in addition to the above options, the Housing Commission at its April 9 workshop outlined two process items for

consideration. The first calls for creating a rating system to determine a project's overall benefit to lower income households (for example, relationship to transportation, percentage of inclusionary units, project amenities, units for disabled households). This system could be developed along the lines of the State's tax credit application evaluation system that looks at similar key factors as part of the tax credit awarding process. It should be noted that as part of the Housing Element update, staff did rate each high density site and determined its suitability for tax credits. As a result, while this process could provide benefit as a means of weighing a project's overall benefits, its application may be difficult in practice.

The second process change would be to require that all affordability proposals be presented to the Commission at two public meetings. The first meeting would include a project overview and a discussion on the affordability proposal/concepts to allow for public comment and for the Commission to provide feedback for staff and developer consideration early in the review process. The second meeting would be to review the affordable housing and final terms of affordability. The Commission sees this approach as being similar to the Planning Commission's utilization of workshops to conduct a preliminary review of a proposed development. In the past, staff has attempted to present projects on more than one occasion; however, developers have expressed dissatisfaction with this approach as it disrupts the project review timeline and is inconsistent with Palmer.

Finally, the Commission also urged staff to promote state legislation that can reverse the impacts of Palmer and establish new criteria for affordable housing. As an example, Assembly Bill-1229 would allow for cities to adopt ordinances regulating zoning that include inclusionary zoning as a condition of development approval.

As part of the workshop, the City Council may want to comment on these matters and direct that they be included as part of the IZO amendment process.

Timeline

Depending on the City Council direction provided at the workshop, staff anticipates it could provide a general report to the Housing Commission at its June/ July meeting and that there would be at least one additional public meeting to review final draft language. Staff also assumes that the final draft documents would also be forwarded to the Planning Commission and/or the Economic Vitality Commission for comment. As such, a final document may be available for City Council for its action in September/October.

Direction for Interim Affordable Housing Standards/Process

Due to concerns related to *Palmer*, staff has taken a cooperative approach with the St. Anton, California Center and the Auf der Maur projects in an attempt to both identify incentives that result in an agreement to provide affordable units and to generally stress the importance of affordable housing within the context of the City's Housing Element and the City's *Housing Site Development Standards and Design Guidelines*. As evidenced with the California Center project, this approach resulted in 15% rent restricted units that are at higher income limits than are currently allowed in the IZO.

Discussions with the other two developers have included a range of concepts geared toward obtaining 15% rent restricted units.

In anticipation of St. Anton, Auf der Maur and the Gateway project's (the latter is just now in the preliminary application review process) continuing their application review process, staff has identified three interim negotiation approaches for addressing this situation:

1. Direct staff to adhere to the affordability standards as outlined in the IZO. (This retains legal exposure.)
2. Direct staff to continue to negotiate in an attempt to acquire as much affordability as possible, utilizing an incentive based approach, including financial contributions.
3. Direct staff to focus its work on completing the LIHF nexus study as compared to processing development applications.

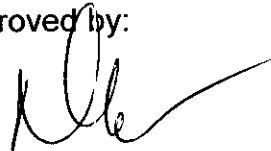
Based on the current legal environment and the results of staff's approach to date, staff recommends a continuance of the current practice as outlined in interim Option 2.

Submitted by:



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Approved by:



Nelson Fialho
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Attachments

1. April 16, 2013, City Council Agenda Report
2. City Inclusionary Zoning Ordinance
3. City Resolution 10-390 concerning Non-Discrimination
4. HUD 2013 Income and Rent Limits
5. April 8, 2013 Letter from Citizens for a Caring Community
6. General Information on state of Inclusionary Housing
7. Legislative summary of AB -1229